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THE TRANSPORTATION & BUSINESS LOGISTICS MAGAZINE APRIL 1987

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RAIL LABOR'S LAST STAND: WHAT'S AT STAKE FOR SHIPPERS?

Computer Systems: How To Pick a Winner

Spanning America For Small Shipment Success Stories

Leasing Services Directory

VOL. 86, NO. 4

CHILTON'S
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APRIL 1987

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THE INTERMODAL MUDDLE

As the response to our February Dialogue question shows, about the only thing shippers agree on regarding intermodal marketing is that there are many viable alternatives. Some of you told us that it was best to deal directly with the railroads, while others laud the advantages of third parties because of their convenience, flexibility and pricing. Still others wish for someone able to capture the advantages of both. The bottom line here seems to be that shippers want to deal with someone who knows the service and has the authority to make rates.

"Intermodal services should be marketed directly by the railroads. Third parties create confusion. Truckload motor carriers are very simple to deal with. That is way their market share has increased."—**Jim Ammons, director, traffic, Baddoua, Inc., Memphis, Tenn.**

"Without great volume, third parties can get you a good price. They offer one billing for door-to-door service as well as complete responsibility—if you insist."-**H. Nicholls, distribution service manager, R. R. Donnelley & Sons, Warsaw, Ind.**

continued

Who markets intermodal services to you now?	
third-parties	75%
railroads	58%
steamship lines	35%
What is your greatest source of confusion when using intermodal services?	
routes/rates	37%
liability	31%
in-transit communication	22%
For intermodal movements today, direct sales calls are more necessary	53%
Intermodal service makes computerization of distribution:	
more difficult	21%
less difficult	8%
no different	71%
In the last two years, the quality of intermodal service has:	
improved	63%
declined	10%
not changed	22%

QUESTION OF THE MONTH

AUDITING THE RATE AUDITOR

Prior to 1980, determining correct rail or motor freight rates was both a complex and expensive task. A lot of corporate overhead was required just to subscribe to traffic-monitoring devices, keep them updated, retrieve rates, and analyze the company's rate uses and patterns.

At that time, things were pretty much manually based, and rate auditing firms often were invaluable in recapturing lost freight expenses.

But today, simpler contracts, tailored LTL service, disk-based rates and sophisticated computer-based rate service firms have changed the role of the traditional rate auditing firm. Yet many exist and thrive.

What has been your experience with rate auditors? Do these services give your firm the "bang for the buck" they once did? What advice do you have for anyone considering using a rate auditor today? What advantages, if any, do audit houses still hold over computerized, in-house systems?

Do you rely on them mainly for pre-audits, or are they primarily enlisted to do post-audits? Or both? Please let us know by filling out and returning the card at the bottom of this page.

DIALOGUE April 1987

- How many freight bills per month are audited:
_____in-house by hand; _____in-house by computer;
_____by auditing firm; _____by outside computer base

- What is your approximate annual freight expenditure?
_____$0 to $100,000; _____$100,000 to $500,000;
_____$500,000 to $1 million; _____$1 million to $5 million;
_____$5 million to $50 million; _____over $50 million

- What percentage of all bills are audited?_____ percent.

- What percentage of all bills are pre-audited?_____ percent.

- Which freight bills represent the largest number of errors (rank the top three)?
_____LTL; _____TL; _____Rail; _____Air; _____Ocean;
_____Third-party; _____Other (specify) _____

- Rate the service of your auditing firm on a scale of 1 to 5 (with 1 representing the best service).
_____volume of bills audited; _____amount of overcharges recovered; _____speed of processing; _____cost of services

The advice I have for other shippers and receivers when selecting or using an outside auditing firm is:

_____

NAME (print) _____ TITLE _____

COMPANY _____ PHONE _____

ADDRESS _____

CITY _____ STATE _____ ZIP _____

FIGURES IN SPEECH

(Quotes from transportation and distribution notables that have caught the ears of *DISTRIBUTION* editors.)

"Unfortunately, instead of looking forward and stretching its minds, this highly distinguished panel framed its discussions in the arguments of yesterday. . . . The majority opinion though recently written, easily could have been penned long before this committee was assembled. . . . This report recommends the perpetuation of activities that had their genesis with the hard rubber tire—tariffs, rate cartels, antitrust immunity. . . . Instead of grabbing the initiative and leading reform or even gracefully acknowledging the realities of transportation in 1987, the Task Force and its report will be perceived as a stonewalling effort and will have a long-lasting adverse affect on the trucking industry. . . .

The Blue Ribbon Force missed a singular opportunity to redirect ATA policies to better arm the motor carrier industry with the tools it needs to be an effective competitor in today's global economy."—**E. M. Cody, distribution manager, GoodMark Foods and president of the Private Carrier Conference, from the dissenting opinion of the ATA Blue Ribbon Task Force on Economic Regulation.**

INTERMODAL MUDDLE continued from p. 7

"I prefer to deal with the rail company; however, the service level at delivery rail heads is still very poor, as is the internal communication with the carrier during the actual move. I get a lot of promises but no action."—**Rod Martin, corporate traffic & distribution manager, DEP Corp., Rancho Dominquez, Calif.**

"I prefer to buy intermodal services from the person who knows what he is talking about. Too often the salesperson really doesn't know the full story."—**Noel Strock, traffic manager, A. J. Hollander & Co., New York.**

"I like to deal with shippers' agents that can provide through-billing, origin to destination."—**R. Engebretsen, division traffic manager, Sta-Brite Industries, Inc., Delavan, Wis.**

"We have found that by using a consolidator or forwarder we can benefit from an all-inclusive service. If drayage or special handling is required, we don't need to shop around for the additional support. This is particularly important when minimal times in transit are scheduled."—**Mike Piercefield, distribution regional traffic manager, AAFES, Forest Park, Ga.**

"Third-party agents are better positioned to market intermodal services. They have a multitude of options at their disposal to present to shippers, and the clout of consolidated voulme to make it work."—**Donald A. Nichols, distribution manager, Guardian Industries, Carleton, Mich.**

"Intermodal services should be offered to shippers by the carrier offering the service. The carrier should have rates in effect with the railroads."—**James D. Black, terminal manager, Lawrence Freight Line, Inc., Lawrence, Kan.**

"I would prefer to have intermodal services marketed directly by the railroads, but at the normally lower third-party prices."—**T. R. Erickson, manager, transportation, Navistar International, Schaumburg, Ill.**

"I would rather deal either directly with a railroad rep *or* a third-party broker *with* a railroad representative."—**Rich DeSantis, traffic manager, Lumex, Inc., Bay Shore, N.Y.**

"I would prefer to deal with an independent broker who deals with many third parties, so as to utilize their various discounts and agreements."—**Darwin George, sales manager, Eagle Systems, Inc., Billings, Mont.**

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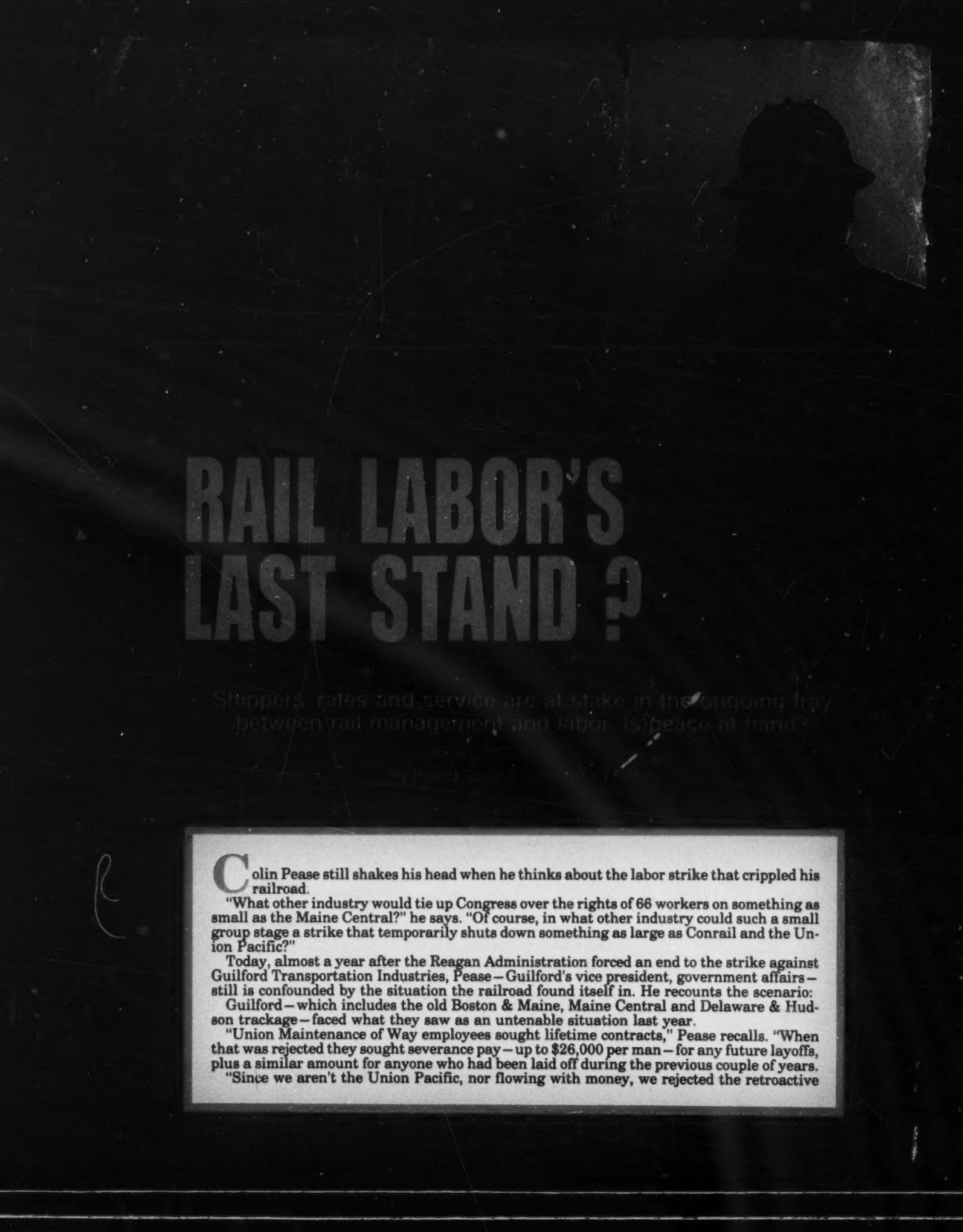

RAIL LABOR'S LAST STAND ?

Strippers, rates and service are at stake in the ongoing fray between rail management and labor. Is peace at hand?

Colin Pease still shakes his head when he thinks about the labor strike that crippled his railroad.

"What other industry would tie up Congress over the rights of 66 workers on something as small as the Maine Central?" he says. "Of course, in what other industry could such a small group stage a strike that temporarily shuts down something as large as Conrail and the Union Pacific?"

Today, almost a year after the Reagan Administration forced an end to the strike against Guilford Transportation Industries, Pease—Guilford's vice president, government affairs—still is confounded by the situation the railroad found itself in. He recounts the scenario:

Guilford—which includes the old Boston & Maine, Maine Central and Delaware & Hudson trackage—faced what they saw as an untenable situation last year.

"Union Maintenance of Way employees sought lifetime contracts," Pease recalls. "When that was rejected they sought severance pay—up to $26,000 per man—for any future layoffs, plus a similar amount for anyone who had been laid off during the previous couple of years.

"Since we aren't the Union Pacific, nor flowing with money, we rejected the retroactive

portion of their demands and they struck."

The strike—which resulted in the secondary picketing case that is now before the Supreme Court—caused the railroad to withdraw earlier offers and hire 1,200 new people to run the line.

"It took two months to get it running—and ultimately caused the loss of close to $100 million in annual revenues," says Pease, "but it allowed us to structure the railroad in a way that seems to make competitive sense."

A Big Impact

Though its ranks have shrunk by more than a third since 1980, American rail labor remains the industry's great floating variable. Employment has fallen from approximately 532,000 to 345,000, according to figures from the Association of American Railroads. Despite this, rail labor still accounts for roughly one-half of a line's operating expenses. And that means that, directly or indirectly, the cost of labor impacts upon every shipper's rail rates

continued

and service levels.

The largest, Class One railroads, those with $84 million or more in annual revenues, divest themselves of unprofitable stretches of track—determinations made with labor costs and manning requirements in the forefront. New innovations and streamlined services hit the rails—but only after specific agreements, usually including relaxations of standard crew sizes, wage structures or work rules—are ironed out. New lines—dubbed short lines, feeder railroads or regional railroads—sprout from the unwanted Class One trackage. But these newcomers are born only through labor arrangements differing radically from those in effect on the Class One lines.

Therefore, the one question underlying most railroad discussions is, what will labor do to stem its rate of attrition? Will it continue to show levels of flexibility that have enabled a number of new services to capture traffic back from the highways? Can labor be convinced that by working to increase profitability, jobs might actually be added? And, how do these decisions affect shippers, the ultimate transportation mode decision makers?

Among the larger lines, one of the most cogent answers to these questions came from John P. Frestel, Jr., vice president-personnel and labor relations for the Atchison, Topeka and Santa Fe Railway Co.

Santa Fe is one of many railroads performing a high-wire act these days. They are required to continually search out cost savings—including work force cuts—while boosting revenues with the remaining staff.

"We have too many people in the operating crafts, and too many people in clerical positions," says Frestel. "You don't need five people to operate a modern train. And you don't need the large volume of clerical people, many of whose former tasks are now handled by computer systems."

Santa Fe's employment roster, which peaked in 1981 at 34,800, fell to 21,100 by January 1987. Those figures include a reduction in clerical staff of 5,000 during the same time frame. "And though we're not happy about it," Frestel adds, "we're not through yet."

Some Strategic Successes

The relationship between rail labor and management has not been without bright spots, though. One of the things Frestel is happy about, for example, is the addition of 117 railroad jobs on the Santa Fe's new Quality Service Network (QSN), which debuted last October.

The trains use three-man crews on runs linking 15 city pairs six days a week. "This service is cost-effective because we didn't have to man it under existing labor agreements," Frestel emphasizes. "Under those rules we would have had to add an extra 55 jobs—and that would not have allowed us to create the new service."

The service also features larger crew districts, allowing the trains to run longer before stopping for crew changes. This makes for faster transit times. Which makes shippers happy.

Typical of its success is the 35-hour, 40-minute Denver-to-Houston schedule that competes directly with over-the-road service. Here, labor agreed to regard that passage as operating over five instead of 10 crew districts. Under agreements negotiated with the Brotherhood of Locomotive Engineers and the United Transportation Union, the new trains also operate over longer crew districts, averaging 286 miles, with the longest being 335 miles.

"Without these agreements," Frestel adds, "the trains would not be cost or service-competitive with trucks."

Union Pacific has experienced similar success with its new intermodal "Sea-Port Fast Track" service connecting Seattle and Portland. Minus cabooses and fire-

COMPENSATION TO REVENUES AND HOURS PAID TO HOURS WORKED

Railroad	Compensation as % of Revenues	Hours Paid for/ Hours Worked
Baltimore & Ohio	39.5	1.15
Chesapeake & Ohio	41.1	1.15
Seaboard System	32.2	1.28
Norfolk & Western	32.6	1.21
Southern Railway	30.8	1.21
Conrail	32.1	1.25
Burlington Northern	28.1	1.29
Missouri Pacific	31.4	1.33
Union Pacific	37.8	1.36
Santa Fe	36.5	1.35
St. Louis Southwestern	27.0	1.39
Southern Pacific	35.5	1.37
Florida East Coast	21.1	1.05
Class I	33.4	1.28

Source: Association of American Railroads/E.F. Hutton (1985 figures)

Major railroads still suffer from unrealistic work rules that require payment for more hours of work than are actually performed. Only the non-union Florida East Coast gets close to an hour's work for an hour's pay, but it took a bitter strike for the FEC to achieve these gains. It is unlikely that other major railroads will enjoy similar improvements in work rules any time soon, even if one or more was willing to take a strike. Binding arbitration and Congressional pressure would likely end such a strike before any work rule changes were forced on the unions.

men, the service is targeted to recapturing truck traffic on the 183-mile run.

"Overall, labor gained two workers who otherwise would have been furloughed," says Tom Watts, vice president, labor relations and personnel. "They decided it was better to have two actual people on the job, than four theoretical people looking at the wall."

'Fiscal Frankness' With Labor

The daily trains are running, in part, because of what Watts describes as complete fiscal frankness with labor—including opening the corporate books to spell out the financial realities.

"Before we initiated this service, we carried virtually nothing between Seattle and Portland except for freight heading somewhere else," says Watts. "With underutilized tracks and cars, we needed labor's cooperation to make a win/win situation."

At Burlington Northern, Vice President, Labor Relations James Dagnon says that his line's two-man crew, 30-car intermodal Expediter trains are the "biggest success we've had" in recent years. The Expediter, too, was the result of specific labor negotiations. But, Dagnon says, it also reflects a genuine effort on BN's part to get the corporate point of view out to its 35,000 employees.

"We created a lengthy video tape featuring a hypothetical company that clearly is meant to represent Burlington Northern," Dagnon says. "In it we show how we need to increase volume, cut costs or both, in order to get to the point where investors seeking a reasonable 10 to 12 percent return on investment could find such an opportunity in a railroad.

"The tape points to the conclusion that since there isn't much chance for a boost in volume or prices, there simply has to be greater return on investment from our labor force," he adds.

Dagnon says labor is the key, because after computerized rail yards, fuel efficient locomotives, and lighter, more aerodynamic freight cars are all in place, the only available arena for cost savings is labor.

The effort seems to be paying off. "Burlington Northern's Expe-

continued

RAILROAD EMPLOYMENT BY JOB CATEGORY

	1985	1975	% Change
Executive, Officials & Staff Assistants	13,326	16,704	−20.2
Professional & Administrative	52,034	102,646	−49.3
Maintenance of Way & Structures	51,473	81,507	−36.8
Maintenance of Equipment & Stores	52,740	104,578	−49.6
Transportation (excluding train & engine)	18,671	27,062	−31.1
Transportation—train & engine	87,405	155,263	−43.7
Total	275,649	487,759	−43.4

Source: Association of American Railroads/E.F. Hutton

Railroads have made concerted efforts to reduce employees in recent years. Total rail employment tumbled 43.4% from 1975 to 1985. The largest drops were among maintenance workers (−49.6%), professional and administrative workers (−49.3%) and train and engine employees (−43.7%).

diters are absolutely dynamite," says Mark Smith, who heads Hub City Kansas City Terminals, Inc.

"I'm a large truckload broker, as well as an intermodal shipper, looking for the best deal for my customers," he says. "A shipper tells me what he wants to spend and the service he requires, and I buy that service for him. Due to innovations like the Expediter, railroad traffic becomes a more viable choice every day."

More Than a Few Rough Spots

With all these success stories, it might appear that peace and quiet had suddenly settled upon the American railroad scene. This is certainly not the case.

Management still chafes under stipulations of the Railway Labor Act that puts rail regulation in a whole different ball park—some even say a different planet—than other U.S. industries.

For example, secondary picketing—illegal under the National Labor Relations Act—is still being tested in the courts to determine whether it's legal under separate railroad regulations. This practice, where a union pickets a line connecting with one being struck, could paralyze the nation.

And then there is the question of the separate railroad employers liability act which, according to one Chicago-based executive, "might well have been pertinent back in 1912 when it was instituted, but certainly is not so today."

He explains that the separate regulations originated in response to grim conditions on early 20th century railroads. In 1907, for example, nearly 12,000 employees lost their lives on the job.

Today, under these rules, railroad workers retain the right to sue their employers with no limit on possible awards—unlike the no-fault arrangement in effect on everyone else's workmen's compensation policy.

According to the executive, this results in payments of $75 million to $100 million more for the railroad industry operating under the Railway Act than it would under standard workmen's compensation. "While railroad's 46 fatalities in 1985 were 46 too many, we're certainly not as dangerous an industry today, as, say, coal mining," he says. "Yet mine owners don't operate under a separate Coal Industry Labor Act."

EMPLOYMENT AND COMPENSATION

Year	Employees (thousands)	Compensation ($ million)
1944	1,413	3,853
1955	1,058	4,994
1966	630	4,879
1971	544	6,000
1975	488	7,475
1981	437	11,561
1982	379	11,021
1983	322	10,345
1984	323	11,004
1985	302	10,563

Source: Association of American Railroads/E.F. Hutton

Total railroad employment rolls have dropped significantly since World War II, but prior to 1982 the benefits from employee reduction largely went to remaining employees. Since 1981, gross compensation has dropped or remained relatively constant—allowing more funds to be spent on capital expenditures and mechanization.

Other trouble spots include the superior benefits offered rail workers—who get up to 52 weeks of unemployment insurance benefits *plus* the right to benefits while on strike, under provisions of the separate Railroad Unemployment Insurance System.

"What was valid during the early days of the century, when rail was king, is hardly valid today," another source notes. "We need to defederalize our employee relations in order to get onto the same level playing field on which other American corporations compete."

Starting Fresh

The regional railroads mentioned earlier have prospered under these conditions. Frank Wilner, assistant vice president for the Association of American Railroads, notes that these routes—whether union or non-union—do well because they are not tied to such age-old bedrock as payment based on mileage.

"In our last contract, the basis for operating crew payment was raised by 8 percent," explains Wilner. "That means they get paid a day's wage for every 108, instead of 100 miles, they work. But that still means someone can easily get paid three days wages for one day's work. That's typical of the things new feeder lines specifically avoid."

Because they are whole new entities, the regional or feeder lines are basically free to set their own work rules. And there are a number of success stories among these lines, too, to show that starting fresh pays benefits not only to management, but to labor as well.

Consider the Chicago, Central & Pacific which, on January 23, announced that workers would receive *bonuses* of between $200 and $500, based on a good showing in the line's first fiscal year.

John Haley, chief executive officer of the 772-mile line—formerly part of the Illinois Central Gulf—says the key was "productive labor and aggressive marketing. You can't succeed without both."

Daily wage rates, two-man crews, and a cooperative attitude are prime factors in what Haley cites as a truly unique phenomenon: "We've been in business for just 15 months and we're the only U.S. railroad to recently hire trainmen. With smaller crews we ended up with fewer people per train—but many more trains." As a result, employment is up sharply at CC&P, and while its $60 million in revenue is a drop in the bucket compared to many Class One railroads, Haley's group made money and added people last year. Most of the Class One lines did not.

"We've seen a lot of shippers coming back to the line, shippers moving everything from intermodal goods to grain, lumber, frozen meat and ties," adds Haley. "One sign of our success is that we've had to add five intermodal ramps to the four that were there when we opened."

Another ICG offshoot is Mid-South Rail Corporation, which operates a 308-mile route from Meridian, Miss. to Shreveport, La., plus a 70-mile link from Hattiesburg to Gulfport, Miss.

There, says ceo Edward Moyers, "the first thing we did was to reach agreement with labor that allows us to produce a level of productivity that keeps us competitive in the marketplace." As a re-

sult, two and three-man crews, and maximum flexibility in shops, are *de regieuer* at MidSouth.

"In our locomotive repair facility we can use people that belong to different craft organizations to do a wide variety of work," says Moyers. "A mechanic can do electrical work, a carman can do a machinist's job—they can step across formerly strict job description boundaries." That has not only kept labor costs down but, Moyers adds, "we've had an extremely low bad order ratio," referring to the number of locomotives in the shop for repairs vs. the number on the job. "We never just wanted to slash costs. We truly want everyone to enjoy a good standard of living. But that's only possible if the line is successful."

So far, that seems to be the case. Rates on the year-old line have attracted cargo back from trucks, and Moyers claims he even heard bargemen at Vicksburg, Miss. complain that MidSouth had taken all *their* business as well.

Labor Leaders' Worries

With major contracts running through the current calendar year, relative labor peace is to be anticipated. Indeed, what seems to worry G. Thomas DuBose, vice president of the United Transportation Union, and R.P. McLaughlin, vice president of the Brotherhood of Locomotive Engineers, is the size of the employment base supporting railroad retirement and other contributory programs. DuBose' union represents conductors, brakemen, yardmen, firemen and engineers. He says he never anticipated membership dropping below 350,000. "But now," he says, "we're below 300,000, and with all the mergers and technology, that total could easily get to 200,000."

What does labor see as the root of the dilemma facing the railroads? DuBose says one problem is that big railroads aren't that interested in railroading anymore.

"They're all concentrating on selling mufflers and candy bars, or operating mines, barges, ship lines, and even airlines," he says. "If they could get back to basics, emulate the small lines, and serve all the customers, railroads could easily pick up 15 to 20 percent more business. And that would almost be enough to bring back all the furloughed employees."

"They're all concentrating on selling mufflers and candy bars, or operating mines, barges, ship lines, and even airlines. If they could get back to basics, emulate the small lines, and serve all the customers, railroads could easily pick up 15 to 20 percent more business. And that would almost be enough to bring back all the furloughed employees."

G. Thomas DuBose, Vice President, United Transportation Union

McLaughlin has seen BLE membership drop from 38,000 to 30,000 in the past six years, yet he feels membership levels—and the railroads' loss of freight to other modes—is stabilizing.

He's dubious, though, about productivity claims, particularly increases in piggyback traffic. Much of these gains, he says, is not so much new traffic as freight that used to move in boxcars, then moved to the highways, and now is riding piggyback. He also resents engineers being grouped with other rail workers when counting crew sizes. "Asking engineers to increase productivity usually means asking them to haul trains that are twice as long with no more than a dollar a day in extra compensation," he says.

Correctly gauging and halting slack between cars is much more difficult on longer trains, says McLaughlin, and compensation should reflect that extra effort.

Reason For Optimism

How does all this impact on the shippers?

Terry L. Priest, manager of transportation and physical distribution at Adolph Coors Co. Brewing Division in Golden, Colo., says "the cabooseless trains we see are a good example of the way that lines like the Santa Fe are getting their rates competitive with other modes."

Russ Shores, corporate traffic manager of Brown Printing Co., has seen service improve on inbound paper shipments to its home base in Waseca, Minn. Brown receives about a hundred railcar shipments a month, and since the Chicago & North Western sold part of its route to the new Dakota, Minnesota, & Eastern, "we are now able to get the switches or deliveries we need." Before, he recalls, "some days we couldn't get any deliveries, and that often caused a real bunching of cars and a stiff demurrage bill from the railroad.

"Now, though, the DM&E is giving us two switches a day, and that's really helped us solve that problem." The DM&E, he adds, offers this service with cabooseless, two-man trains—compared with the former line's four-man crews.

At the U.S. Foods Division of Pillsbury, Joe Fall, Northern Iowa area manager for grain merchandising says: "More and more, we're relying on rail to bring our goods to river barges." Fall's group is the "commodity knowledgeable" branch of the huge corporation, responsible for pricing transportation for corn, wheat, soybeans and other bulk products. Since freight rates are a critical part of any sale, Fall has good reason to be encouraged by the performance of the feeder lines.

"We've seen one of those ICG spinoff lines come in, reduce crew sizes from five to three, eliminate feather-bedding, pay the crew well, and even give them bonuses for good service. And with all this the line's rates have dropped. That's made us really pay attention to what they're offering."

Where all of this leads is open to question. One thing, though, is certain. Whatever lies ahead for the nation's railroads will, to a great extent, be determined by two critical elements: The needs and fears of America's railroad workers, and management's ability to blend labor's goals with its quest for profitability. ★

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KNOW YOUR DISTRIBUTION COSTS

The internationally known consulting firm of Herbert W. Davis and Company teams up with DISTRIBUTION to bring you DATABASE, an ongoing, comprehensive report of key distribution costs.

How much does distribution cost your company as a percentage of sales? How does this compare with other companies? Or, looking at distribution positively, how much does distribution contribute to the firm's bottom line?

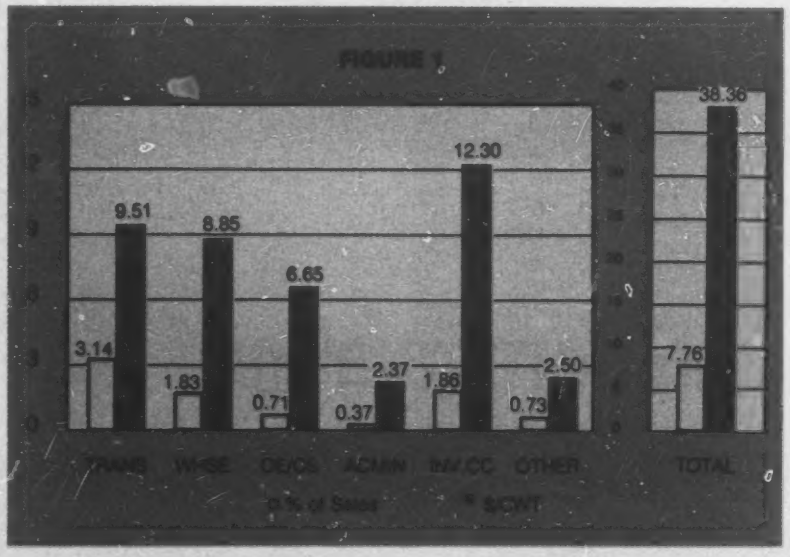
In these days of managing by the numbers, transportation and distribution managers have to have the answers to these questions. While many distribution departments have developed systems for tracking their own costs, gathering average distribution cost figures or comparative cost figures for their specific industry is difficult if not impossible.

Help has arrived.

DISTRIBUTION Magazine and the consulting firm of Herbert W. Davis and Company have teamed up to provide our readers with on-going, comprehensive distribution cost information. In the months to come, DISTRIBUTION will report on actual average costs experienced by at least 300 major U.S. companies, including specific costs for transportation, warehousing, order entry, customer service, inventory control, administration, and other elements of total distribution cost.

Herbert W. Davis and Company has been gathering this distribution cost information for 12 years and has developed the most comprehensive database of its type in the world. DISTRIBUTION will be bringing this information to its readers on an ongoing basis as the DATABASE

The figures in this installment of the DATABASE represent costs gathered in 1986. Future installments in DISTRIBUTION will include 1987 costs. Indeed, DISTRIBUTION readers have the opportunity to participate in this information and receive detailed, personalized and confidential comparative cost information (See the box on p. 39).



The DATABASE measures distribution costs in two ways: as a percentage of sales revenue and as a cost per hundredweight. The average corporation in the 1986 DATABASE posted sales of $588 million. The average volume shipped was 800 million lbs., and the the average sales-value-per-pound was $6.64.

Looking at overall figures, the average total distribution cost was 7.76 percent of sales revenue. This means that a company with $500 million in sales recorded distribution costs of almost $40 million and a per hundredweight cost of $38.36 (See Figures 1 and 2)

Transportation continues to be the largest distribution cost component, representing about 37 percent of total distribution costs and 3.14 percent of sales revenue. Inventory carrying costs and warehousing ranked second and third respectively in expenses as a percentage of sales--at 1.86 and 1.83 percent. The inventory figure was calculated on an 18 percent cost-to-carry basis.

While transportation costs are on the downswing, inventory and warehousing expenses are moving upward. Several years ago, inventory and warehousing costs represented only 20 percent each of total distribution expenses. Today, they figure as high as 25 percent.

Cost figures vary somewhat for specific industries. High-value pharmaceuticals, for instance, show the lowest percent-of sales cost—3.44 percent. On the other hand, industrial non-durable goods are near the top of the percent-of-sales cost table at 9.19 percent (See Figure 2).

Looking at distribution cost trends since 1980, we see they declined during each of the past five years. The largest decreases occurred during the last three years with drops of 7.8 percent in 1986, 3.7 percent in 1985 and 6.4 percent in 1984 (See Figure 3).

continued

FIGURE 2

	% of Sales	$/CWT
All Companies	7.76	38.36
Industrial Non-Durable	9.19	38.74
Chemicals	7.73	4.52
Hospital	8.16	83.01
Industrial Durable	7.08	43.93
Industrial Durable < $5/lb.	6.71	14.93
Industrial Durable > $5/lb.	7.49	76.15
Consumer Non-Durable	6.86	35.43
Food Products		
Dry and Packaged Food	7.28	5.88
Canned and Processed Food	7.61	4.29
Temperature Controlled Food	8.41	7.39
Non-Food in Grocery Channel	7.60	44.83
Pharmaceuticals < $10/lb.	4.95	29.83
Pharmaceuticals > $10/lb.	3.44	130.51
Consumer Durable	9.35	45.21
Retail Stores	8.26	27.09

FIGURE 3

DISTRIBUTION COST IN

	% of Sales	$/CWT
1986	−7.8%	−4.6%
1985	−3.7	+3.3
1984	−6.4	−8.3
1983	−1.4	+6.1
1982	−0.8	+7.6
1981	−0.5	+5.3

FIGURE 4

	1986-85 Percent Change In	
	% of Sales	$/CWT
Finished Goods Transportation	−6.3	−1.6
Warehousing	−10.6	−6.3
Order Processing/Customer Svc.	+4.6	−0.3
Distribution Administration	+0.3	+3.5
Inventory Carrying Cost @ 18%	−3.8	+0.3
Total	−7.8%	−4.6%

FIGURE 5

DISTRIBUTION EXPENSE AS A PERCENT OF SALES

By Direction	% of Companies	% Change
All	100%	−7.8%
Held Steady	27	0.0
Reduced	59	−16.8
Increased	14	+16.4

DISTRIBUTION COSTS PER HUNDREDWEIGHT

By Direction	% of Companies	Avg. % Change
All	100%	−4.6%
Held Steady	31	0.0
Reduced	44	−20.7
Increased	25	+17.3

Within the categories measured by the database (transportation, warehousing, etc.) there are definite trends over the last three to five years. Finished goods transportation saw a 21 percent cumulative cost decrease since 1981. Warehousing recorded a 16 percent cost decrease since 1981 reflecting successful efforts to cut inventory and improve productivity. Inventory carrying costs have dropped about 28 percent since 1983 due largely to increasing use of just-in-time stocking strategies and low interest rates (See Figure 4).

Not all distribution costs are going down. Order entry and customer service expenses rose five percent in 1986 and increased three to 10 percent every year since 1981. These increases are apparently the result of companies handling a larger volume of smaller orders, which requires more customer service personnel and cost. Additionally, competitive pressure is forcing higher quality and excellence in service, which in turn requires beefed up customer service departments and procedures.

Distribution administrative costs are rising as well, up 0.3 percent over 1985. This increase is apparently caused by firms using administrative people to reduce costs in transportation, warehousing and inventory areas.

The most important statistic to come out of the Davis DATABASE in 1986 is the fact that participants trimmed their distribution cost as a percent of sales by more than two percent from 1985. Average distribution costs dropped from 9.8 percent in 1985 to 7.76 percent in 1986. A closer look at the numbers, however shows major variances in cost-reduction performance (See figure 5). Specifically, 59 percent of the participants reduced costs by 17 percent; 14 percent saw cost increases of 16 percent; and, 27 percent remained unchanged.

These variations mean the winners have a 33 percent competitive advantage over the losers in terms of distribution costs in 1986. That 33 percent profit differential translates into a substantial three percent profit contribution to the bottom line as compared with losers.

In terms of cost-per-hundredweight, 31 percent of the participants held costs steady in 1986; 44 percent reduced costs by 20 percent; and, 25 percent increased costs by 17 percent. The differential between the cost-per-hundredweight winners and losers therefore is 38 percentage points.

The two to three percent bottom-line contribution is a very significant number. Consider that a number of industries only earned two to four percent profit in 1986. Distribution savings made the bulk of the profit for these companies in 1986.

BE A WINNER IN THE BATTLE FOR LOWER DISTRIBUTION COSTS

The average participant in the 1986 DATABASE lowered distribution costs by two percent. How does your company compare?

Herbert W. Davis and Company invites you to participate in the 1987 cost study to find out. Participants in the study will receive detailed reports that compare their distribution costs with the averages for their particular industry. There is no cost for participation. All you have to do is fill out the adjacent cost reporting form, and a corresponding customer service form in next month's issue of DISTRIBUTION, and return both to Herbert W. Davis and Company.